



Final Minutes
Endowment Fund Investment Regular Board Meeting
November 16, 2010

A regular meeting of the Endowment Fund Investment Board (Board) was held in the Board Conference Room at 816 W. Bannock Street, Ste. 301, Boise Idaho on November 16, 2010. Chairman M. Dean Buffington called the meeting to order at 9:03 a.m. and recognized that a quorum was present.

Member's Present:

Dean Buffington
Gavin Gee
Representative Max Black
Vaughn Heinrich
Tom Kealey
Sue Simmons
Richelle Sugiyama
John Taylor
Senator Chuck Winder (*arrived at 9:34 a.m.*)

Staff Present:

Larry Johnson
Chris Halvorson
Andy Potter
Judy Shock (*arrived at noon*)

Legal Counsel:

Julie Weaver, AG

Guests:

Robert Schmidt, Milliman (*departed at 9:36 a.m.*)
Peter Schmole, Harris (*departed at noon*)
Janet Becker-Wold, Callan
Roland Gammill, JRF (*departed at 9:36 a.m.*)
Rhet Hulbert, Clearwater (*9:30 a.m.-12:30 p.m.*)
Eric Jensen, Clearwater (*9:30 a.m.-12:00 p.m.*)
Kathy Opp, Lands (*11:06 a.m.-2:00 p.m.*)

Hard copies of board materials were mailed and delivered seven days prior to the scheduled board meeting and a meeting notice and agenda was posted on the door of the EFIB office beginning November 9, 2010.

Board Meeting Minutes: *Approved*

Mr. Kealey made a motion that the minutes of the August 11, 2010 regular meeting be approved as submitted. The motion was seconded by Ms. Simmons and approved unanimously.

Judges Retirement Fund Actuarial Valuation

Mr. Johnson introduced Mr. Robert Schmidt, Milliman, the Judges' Retirement Fund's new actuary. Mr. Schmidt reviewed the Judges' plan valuation, as of June 30, 2010. The plan was 70.1% funded but does not have sufficient contributions to amortize the unfunded liability.

Mr. Johnson noted that the EFIB is only the investment manager for the Plan and has no influence over contributions. EFIB staff believes the current asset mix is appropriate given the level of funding and recommends no change in that mix.

Fund Performance

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Endowment Fund: The endowment portfolio posted a 10.3% return for the quarter ended September 30, 2010, 64 basis points above its benchmark, and 12.9% for the last 12 months, 286 basis points above its benchmark. Relative to peers, the fund ranked in the 6th percentile for the quarter and 5th percentile for the year relative to public funds (6th percentile for the quarter and 10th percentile for the year relative to endowments and foundations).

Judges' Retirement Fund: The JRF portfolio posted a 9.9% return for the quarter ended September 30, 2010, 7 basis points below its benchmark, and 10.7% for the last 12 months, 9 basis points above its benchmark. Relative to public fund peers, the fund ranked in the 13th percentile for the quarter and 31st percentile for the year.

State Insurance Fund: The SIF portfolio posted a 3.5% return for the quarter ended September 30, 2010 and 7.4% for the last year, versus benchmarks of 3.6% and 7.6% respectively.

Ms. Becker-Wold stated that Mr. Kloepper and she will be meeting with staff in December to discuss strategic options for the plan. Mr. Johnson said board members are welcome to attend.

Ms. Becker-Wold discussed an organizational change at Met West Capital Management. Callan's recommendation is that Met West should be terminated and replaced because the Chief Investment Officer of the EFIB's strategy has departed. With the key portfolio decision maker leaving, there is concern about the continuity of the investment process. In response to a question from Ms. Sugiyama, Ms. Becker-Wold stated, and Mr. Johnson agreed, that the EFIB's portfolio is not in immediate danger because the remainder of the portfolio team is still with the firm and the style is one of very low turnover. Staff and Callan will begin a search process and report to the board in February.

The Board recessed at 9:55 a.m. to attend the Land Board meeting.

The Board resumed at 10:58 a.m.

The Board reviewed the compliance reports.

Mr. Buffington congratulated staff on the quality of the Financial Statements and related audit report for FY 2010, as reported to, and noted by the State Land Board in their meeting just concluded.

Global Equity Implementation

Mr. Johnson described that the final step of the approved plan to increase international equity to 30% of the portfolio, adding \$50 million to the two Global Equity managers, Aberdeen and Lazard, remains to be implemented. He stated that the outlook for international equity remains unchanged from when the strategy was first approved.

Ms. Sugiyama made a motion to approve final funding, within the next 60 days, of the two Global Equity managers for \$25 million each. The motion was seconded by Mr. Kealey and approved unanimously.

Clearwater Rebalancing/Equitization Process

Mr. Johnson discussed the rebalancing and equitization process provided by Clearwater Advisors. Staff has reviewed the process and determined that over all, it contributes a small amount of return from equitizing cash (15-20 basis points, or \$2 million/year) while reducing overall portfolio risk. He stated that staff recommends to continue this program with Clearwater Advisors.

Mr. Gee asked about hidden risks of the overlay process. Mr. Johnson responded that the overlay is implemented using futures, which have large inherent leverage. Therefore, it is critical that a manager have strong internal control over the trading process to prevent any errors, and in staff's opinion, Clearwater has strong internal controls.

In response to a question from Mr. Kealey, Mr. Hulbert indicated that there are appropriate futures contracts available to adjust any over/under weights in international equities.

The Board discussed the rebalancing/equitization process and the consensus was to continue the process and continue using Clearwater Advisors to provide that service for the endowment fund.

Callan Contract

Mr. Johnson indicated that at the August meeting, the Board requested that the inflation escalation portion of Callan's contract be renegotiated. He presented the outcome of those negotiations.

Ms. Sugiyama made a motion to modify the existing contract with Callan to provide that, beginning July 1, 2011, fees escalate at no more than zero and more than the rate of inflation or 3%, whichever is less. Inflation would be measured from June to May. The motion was seconded by Mr. Kealey and approved unanimously.

Update on Securities Lending

Mr. Halvorson shared with the Board that since 2004, net of losses and support payments, securities lending has earned the Endowment Fund \$2.6 million and the Judges' Retirement Fund \$334,040. Overall lending income is down and there have been no significant changes in the structure of securities lending. Staff sees no reason to resume lending. Northern is dropping the direct lending ceiling in an incremental manner, so the Endowment Fund and Judges' Retirement Fund may be out of all securities lending by the end of December. The Endowment Fund has already exited indirect lending.

Approved Strategy for State Trust Land Assets

Ms. Opp stated that on October 19, 2010, the Land Board approved a mid-term strategy for state land assets, the cornerstone of which is to focus land acquisition efforts on commercial real estate, with funding most likely to come from the sale of residential real estate. She also discussed plans to enhance performance of existing non-timber assets, with the overall objective of growing income from \$5 million to \$40 million over the next 20-30 years, while at the same time enhancing the value of timberlands.

The Board recessed for lunch at 12:10 p.m.

The Board meeting resumed at 12:25 p.m.

EFIB Staff Reports

Parks & Recreation Endowment Funds – Mr. Halvorson reported that through the 3rd quarter, the Ritter Island Endowment Fund was up almost 5% and the Trail of Coeur d'Alenes Endowment Fund was up 2%. He indicated that lower cost, non-lending alternatives to current Vanguard index funds have been developed at Northern Trust, which will save Trail of the Coeur d'Alenes endowment about \$1,700/year.

Mr. Heinrich made a motion to change from Vanguard to Northern Trust for the management of the Barclay's Capital Aggregate and TIPS mandates for the Trail of Coeur d'Alenes Endowment Fund and to move Ritter Island's Barclay's Capital Aggregate from Northern's lending fund to their non-lending version. The motion was seconded by Senator Winder and approved unanimously.

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Market Value Report, Expense Report, Coverage Ratio, Land Revenues vs. Forecast, and YTD Land Revenues – Mr. Potter reviewed these reports and Mr. Johnson delivered a detailed report on expenses for the 3rd quarter prepared by Ms. Shock, as a sample of what is available, upon request, for the Board's review. Mr. Buffington reminded the Board that he reviews all travel expenses and approves, in advance, all travel by the Manager of Investments.

Timber Market & School Bond Guaranty Update – Mr. Johnson reported on the US Housing Starts, Inland Lumber Price and Six-Month Average Stumpage Price. He delivered an update on the School Bond Guaranty.

Gift Log – Mr. Johnson reviewed the Gift Log.

Upcoming Issues – Mr. Johnson reiterated the December 1st meeting with Callan to discuss the endowment portfolio, considering current issues and relevant options. He added that board members are welcome to attend this meeting.

Distribution Policy – Superintendent's Questions

Mr. Johnson reviewed proposed responses to inquiries from the Superintendent of Public Instruction related to the Distribution Policy and investment management. The EFIB discussed the items presented and gave staff direction on changes to make before the responses are given to the Land Board.

Adjournment

There being no further business to come before the Board, Mr. Kealey made a motion to adjourn, seconded by Ms. Simmons, and passed unanimously. The meeting adjourned at 2:00 p.m.